

NO FOREIGN DISSEM

CIA/RR CB 65-76
December 1965

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INTELLIGENCE BRIEF

THE DEEPENING BANANA CRISIS IN ECUADOR

DIRECTORATE OF INTELLIGENCE

Office of Research and Reports

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THE DEEPENING BANANA CRISIS IN ECUADOR*

Summary

During the first eight months of 1965, Ecuador's receipts from banana exports, which account for nearly 60 percent of the country's export earnings, totaled only US \$48 million, a drop of \$9 million, or 16 percent, from earnings in the corresponding period of 1964. This decrease was offset by a boost in other exports. However, a sharp rise in import expenditures resulted in a loss of 40 percent of the country's international reserves during October 1964 through June 1965.

The drop in earnings from exports of bananas is in part a result of the resurgence of banana production at formerly disease-infested plantations in Central America and storm-damaged plantations in Taiwan -- areas that possess competitive advantages over Ecuador for supplying markets in the United States, Western Europe, and Japan. These developments illustrate the recurring plight of Latin American nations that depend heavily on a narrow range of commodity exports to earn foreign exchange.

To stop the decline in banana export earnings, the government of Ecuador has attempted to stabilize banana export prices, to reduce export costs, and to develop new export markets through barter trade with Communist countries. In the face of estimates that foresee world consumption of bananas lagging behind rising world production, however, the prospects for mitigating the declining export earnings are not bright. As a result of the drop in export receipts during 1965, Ecuador already is reviewing its projection of foreign exchange earnings from banana exports, since they constitute a major source of financing for the country's National Development Plan (1964-73).

* The estimates and conclusions in this brief represent the best judgment of this Office as of 8 December 1965.

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1. Marked Decline in Banana Exports

The sharp drop in Ecuador's export earnings from bananas is a result of the highly competitive nature of the international banana market. For several years this market has been characterized by the continuous deterioration of banana prices as a result of increased supplies from exporting nations. Through 1964, Ecuador did not feel the impact of declining prices on foreign exchange earnings, because of offsetting increases in volume (see the table). Much of the success achieved in increasing the volume of exports through 1964 was the result of temporary disruptions in the established flow of bananas from other supplier countries to existing markets. Japan, for example, turned to Ecuador for bananas following frost damage to plantations on Taiwan in 1962-63. Japanese imports of bananas rose from a negligible level in 1960-61 to about 16 percent of Ecuador's total banana exports in 1963.

Ecuador: Indexes of Banana Exports
1960-65

	1958 = 100					
	<u>1960</u>	<u>1961</u>	<u>1962</u>	<u>1963</u>	<u>1964</u>	<u>1965 a/</u>
Total value	122	111	121	117	116	99 b/
Price	94	91	89	72	70	70
Volume	130	122	137	162	165	141

a. January-August 1965, using comparable period in 1958 as the base of 100.

b. Estimated.

The recovery of production on Taiwan, however, now threatens Ecuador's banana exports to Japan. It is estimated that exports of bananas to Japan may reach only 835,000 bunches in 1965, compared with a peak of 7.4 million bunches in 1963.

Similarly, the recovery of production in Central America (following the extensive replacement of diseased trees) and in Colombia (following severe storm damage) is reducing Ecuador's share of the banana market in the United States. The increasing availability of supplies from the Caribbean area weakens Ecuador's competitive position inasmuch as Caribbean sources are three to four days closer to US and Western

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European markets and have correspondingly lower transportation costs. For this reason, the United Fruit Co., which accounted for about 15 percent of Ecuador's banana exports in 1964, virtually withdrew from the country's banana market at the beginning of 1965, citing its heavy investments in Central America and Colombia and the advantage of their proximity to the United States. Trade sources also observe that bananas are still considered a luxury product in Western Europe, and despite the acknowledged superiority of Ecuador's product, price is more important than quality.

2. Effect of Falling Exports

The decline in foreign exchange earnings from banana exports has been mitigated somewhat by the favorable performance of the country's other main exports, coffee and cocoa. Preliminary data reveal that in the nine-month period January-September 1965 the total value of Ecuador's exports was \$98.6 million, approximately the same level of export earnings in the corresponding period of 1964.

Despite the offsetting influences of other exports, Ecuador has experienced an alarming decline in its international monetary reserves. After reaching a peak of \$49.8 million in October 1964, the nation's international reserves dropped steadily through June 1965, when they totaled \$31.4 million, a decline of nearly 40 percent. This adverse movement of Ecuador's international monetary reserves is traceable to a sharp rise in import expenditures concurrent with the stagnation in export receipts.

Accompanying the adverse movement of international monetary reserves, fragmentary reports on the domestic economy indicate that during the first half of the year unemployment was on the rise among banana plantation laborers, parking-shed workers, and stevedores, as several large growers and exporters ceased operations. Guayaquil, the country's main commercial center and leading banana exporting port, reported that truck sales had fallen, repossessions were on the rise, and sales in transportation-related industries -- tires, gasoline -- also were being affected.

3. Government Reaction

The government of Ecuador has attempted to counter the sharp drop in banana export earnings in several ways. In the main, the government's actions have been designed to stabilize banana export prices, to

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reduce export costs, and to develop new export markets. To this end, the military junta, in a series of decrees issued since January, has established minimum export prices for bananas, ordered all banana growers to join cooperatives, and directed exporters to buy directly from growers. The government has also negotiated freight rate reductions with Flota Gran Colombiana, a shipping firm jointly owned by semiofficial entities of the Ecuadoran and Colombian governments, following a voluntary reduction by the Grace Line.

As an outgrowth of a program to promote exports in general, and exports of bananas in particular, the government authorized negotiations for barter trade with Yugoslavia, Communist China, the USSR, and the Eastern European Communist countries shortly after the first of the year. Thus far, the only results of the trade mission named to negotiate these barter agreements have been a proposed transaction with Czechoslovakia for two shipments of 150 metric tons of bananas and a reported \$4 million trade agreement with East Germany involving, among other products, an unspecified quantity of bananas. The government's efforts to promote banana exports to Western Europe have thus far led to only small increases in French and Italian import quotas. An additional quota of 10,000 metric tons was granted by Italy as part of an agreement that calls for Ecuador to purchase Italian-built refrigerator ships. The ship order is the result of an agreement signed by the Ecuadoran Government and an Israeli firm, Somerfin Maritime Services, Ltd., which provides for the formation of a jointly owned and operated shipping line to transport Ecuadoran bananas to Italy and European countries, and to return with Israeli cargoes. Under terms of the agreement, four ships are to be constructed, but in the interim, the joint company is making deliveries in chartered ships.

Also under consideration by the government is modification of the 21-percent export tax on bananas. In an effort to reduce costs further in response to the shift toward boxed banana exports, the government authorized banana exporters to manufacture their own boxes despite the protests of existing box manufacturers.

4. Outlook

The immediate prospects for banana exports are not good. Although exporters reported some rise in shipments to Japan, the United States, and Western Europe in September and October, this is believed to be a temporary phenomenon largely due to recent storm damage of plantations in Colombia and Taiwan. Trade sources believed that the recent upturn in export volume would continue until the normal seasonal decline

in November but that the volume involved probably would not compensate for the decline in export earnings during the first eight months of the year.

For the long run, tentative projections indicate that commercial production of bananas will grow faster than consumption. Under these conditions, Ecuador is facing a period of readjustment involving reductions in banana acreage and concentration of production on the most efficient lands in order to reduce costs. Government officials optimistically believe that the industry has about four years to improve its competitive position -- the estimated time before increasing production in Central America and Colombia makes further inroads into Ecuador's markets. The potential of new markets in Communist countries holds some promise, but the quantities imported by these countries probably will not be sufficient to offset the effect of any new inroads into existing markets.

In the light of the developments in 1965, Ecuador's National Planning Board is already reexamining its estimates of foreign exchange earnings from banana exports, since the projected earnings constitute a major source of financing for the country's National Development Plan (1964-73). Whereas the board had forecast that earnings from exports of bananas would increase at an annual average rate of about 3.7 percent during this 10-year period, an independent study estimates that, at best, earnings will increase at about 2.4 percent annually until 1968 and thereafter by about 1.7 percent through 1974. The study concludes that the cumulative shortfall of banana export earnings for the period 1964-73 could be in the range of \$160 million to \$330 million.

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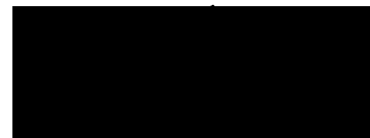
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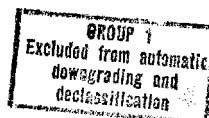
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